

**BEFORE THE  
SURFACE TRANSPORTATION BOARD**

<b>ARIZONA ELECTRIC POWER COOPERATIVE, INC.</b>	)	
	)	
<b>Complainant,</b>	)	
	)	
<b>v.</b>	)	<b>Docket No. NOR 42113</b>
	)	
<b>BNSF RAILWAY COMPANY</b>	)	<b>234872</b>
	)	
<b>and</b>	)	<b>ENTERED</b>
	)	Office of Proceedings
<b>UNION PACIFIC RAILROAD COMPANY</b>	)	September 23, 2013
	)	Part of
<b>Defendants.</b>	)	Public Record
	)	

**RESPONSE OF ARIZONA ELECTRIC POWER  
COOPERATIVE, INC. TO THE BOARD'S JULY 25, 2013 ORDER**

ARIZONA ELECTRIC POWER  
COOPERATIVE, INC.

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Dated: September 23, 2013

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	)	
<b>UNION PACIFIC RAILROAD</b>	)	
<b>COMPANY</b>	)	
	)	
<b>Defendants.</b>	)	
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**RESPONSE OF ARIZONA ELECTRIC POWER  
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Complainant Arizona Electric Power Cooperative, Inc. (“AEPCO”), hereby responds to the decision that the Surface Transportation Board (“STB” or “Board”) served in AEPCO’s rate case against Defendants BNSF Railway Company (“BNSF”) and Union Pacific Railroad Company (“UP”) in NOR 42113 on July 25, 2013 (“*July 2013 Decision*”), regarding implementation of the Board’s decision in *W. Coal Traffic League -- Pet. for Declaratory Order*, FD 35506 (STB served July 25, 2013) (“*Declaratory Order*”).

## I. INTRODUCTION

The *July 2013 Decision* directed the parties to confer and then advise the Board “on approaches to reinstituting the rate prescription” in light of the *Declaratory Order*, which addressed the purchased price adjustment (“PPA”) arising from the 2010 acquisition of BNSF’s corporate parent by Berkshire Hathaway, Inc. (“Berkshire”). *July 2013 Decision* at 3. The *Declaratory Order* directed BNSF to refile its R-1 reports for 2010, 2011, and 2012 “and remove entirely the markup of rail assets due to Berkshire’s non-compliance with 49 U.S.C. § 11323.” *Id.* at 31. The order then allowed BNSF to phase or “transition in the full markup equally over a four-year period, beginning in the R-1 reporting year for 2013.” *Id.* at 2; *see also id.* at 29-31.

AEPCO has conferred with BNSF and UP,<sup>1</sup> and there appears to be general agreement that (a) the rate prescription itself remains at the jurisdictional threshold of 180% of variable costs (*July 2013 Decision* at 3) and should thus be reinstated, and (b) the refiling of the BNSF R-1 reports establishes a need for some adjustment of the rates and reparations that have been paid and will be paid going forward. However, the parties have very substantial disagreement as to the nature and scope of those adjustments.<sup>2</sup> Accordingly, the parties are submitting separate responses to the *July 2013 Decision*.

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<sup>1</sup> The email exchanges between counsel for AEPCO and the defendants are attached as Exhibit A. Counsel also conferred by telephone.

<sup>2</sup> Exhibit B contains a table that depicts the original treatment and the different positions of AEPCO, BNSF, and UP.

## II. SUMMARY

Implementation of the *Declaratory Order* should, in AEPCO's view, entail simply substituting the corrected R-1 data and associated URCS formulas for the original R-1 data and associated URCS formulas that were used, or would be used, at the time. Accordingly, where, for example, the original 2010 BNSF URCS was used to determine the rates and reparations (in 2010-2012), the corrected 2010 BNSF URCS would be used instead. Since the Western Regional URCS was used to cost the Southwestern Railroad ("SWRR") segment on the New Mexico movements, and since BNSF comprises approximately half of the Western Regional costs, the corrected 2010 Western Regional URCS would similarly replace the original 2010 Western Regional URCS. Since there is no revised UP URCS, there would be no changes for UP. The phase-in of the PPA would begin with the 2013 URCS, which would apply during 2015. The full phase-in of the PPA would occur with the 2016 URCS, which would apply during 2018, the last year of AEPCO's current prescription. AEPCO's approach conforms to the *Declaratory Order* and follows the established *OG&E* procedures.<sup>3</sup>

BNSF's approach differs substantially. First, BNSF would substitute the corrected 2011 and 2012 BNSF URCS for the original 2010 and 2011 URCS for use in 2011 and 2012-2013, respectively, apparently because more recent data is now available.

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<sup>3</sup> *Okla. Gas & Elec. Co. v. Union Pac. R.R.*, NOR 42111 (STB served July 24, 2009, and clarified Oct. 26, 2009). The *OG&E* procedures entail a modest delay. For example, the 2010 URCS was also used for the first few weeks of 2013, before the data required to apply the 2011 URCS became available for use in the remainder of 2013. *See OG&E* (STB served Oct. 26, 2009) at 3.

Second, BNSF would not correct the Western Regional URCS for 2010-2011. Third, BNSF would derive a differential between the BNSF portion of the AEPCO costs with and without the PPA for 2010 and 2011, and would begin applying that PPA differential in 2013 (*e.g.*, 25% in 2013, and 50% in 2014). Fourth, as the conventional URCS begins phasing in the PPA with the 2013 URCS, BNSF would employ a reconciliation scheme. For example, BNSF would calculate the 2015 rates using the 2013 URCS (which reflects 25% of the PPA phase-in) combined with 50% of the 2010/2011 PPA differential in order to achieve a total 75% PPA phase-in. The phase-in of the 2010/2011 PPA differential would eventually be reduced and then eliminated to avoid any explicit PPA overrecovery.

BNSF's approach has several fundamental defects. First, nothing in the Board's *Declaratory Order* remotely supports retroactively changing the applicable URCS for a given year or calculating or applying the 2010/2011 PPA differential. The *Declaratory Order* directs BNSF to remove the PPA from the 2010-2012 URCS and then phase in the PPA starting with the 2013 R-1. Second, BNSF's proposal to apply the corrected 2011 URCS to the 2011 rates and the 2012 URCS to the 2012 and 2013 rates amounts to the sort of true-up that the Board precluded in *OG&E*. Third, BNSF's proposal to derive a 2010/2011 PPA differential and then apply it in conjunction with the PPA URCS phase-in directed in the *Declaratory Order* is convoluted, prone to inaccuracy, and devoid of support in the Board's orders. Fourth, BNSF's objection to correcting the 2010-2011 Western Regional URCS is unsupported and would result in excessive rates. Accordingly, none of BNSF's approach can be adopted.

UP's position addresses only 2010 and 2011 (since UP established a proportional rate starting in 2012).<sup>4</sup> UP's view is that the Western Regional URCS should not be corrected, but the original 2011 Western Regional URCS and 2011 UP URCS should apply in calculating the 2011 reparations, even though the 2011 reparations were originally calculated using the 2010 URCS.

UP's position is defective. The *Declaratory Order* addresses only BNSF and provides no basis to change the treatment of UP. UP's (and BNSF's) substitution of 2011 for 2010 would undermine finality in Board determinations and present the sort of true-up that the Board rejected in *OG&E*. There is also no basis to substitute the original 2011 Western Regional URCS for the original 2010 Western Regional URCS for use in 2011 when both are tainted by the BNSF PPA.

Accordingly, the Board should adopt AEPCO's approach. These matters are discussed further below.

### **III. AEPCO'S POSITION**

AEPCO believes that implementation of the *Declaratory Order* should be simple and straightforward:

- First, where there is a corrected R-1 and a corrected URCS (2010-2012), the PPA-tainted URCS should be replaced by the corrected URCS for that year on a *nunc pro tunc* basis. For example, rates and reparations that were calculated using

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<sup>4</sup> UP appears to reserve the ability to take a position on the post-2011 period depending on the outcome of AEPCO's appeal of the proportional rates to the D.C. Circuit. Apparently, UP wants to be able to select the approach that is most advantageous at that time.

BNSF's original 2010 URCS should be recalculated using BNSF's corrected 2010 URCS. The same is true where the 2011 URCS was utilized.

- The 2010-2011 Western Regional URCS should be corrected and replaced in the same manner as the BNSF URCS because the original Western Regional URCS reflects the BNSF PPA found to be improper in the *Declaratory Order*. The 2012 Western Regional URCS should similarly reflect the corrected 2012 BNSF R-1.
- The phase-in of the PPA should be accomplished in a manner consistent with the *Declaratory Order* and the established *OG&E* procedures. The phase-in would begin with 25% of the PPA being recognized in BNSF's R-1 for 2013 and the associated BNSF and Western Regional URCS for 2013. The 2013 URCS would, in accordance with the Board's normal procedure and the parties' established schedule, first be available for use in establishing AEPCO's rates for the first quarter of 2015. There would be an additional 25% PPA phase-in in the following years, with the full PPA being included in the 2016 URCS, which would apply during 2018, the last year of AEPCO's rate prescription.

The above approach conforms fully to the *Declaratory Order* and the established *OG&E* procedures. The *Declaratory Order* disallowed all of the PPA in the BNSF R-1 Reports for 2010, 2011, and 2012, and directed that the PPA be phased-in equally in the BNSF R-1 Reports for 2013-2016. In the normal scheme, the R-1 report for a given year forms the basis for the URCS for that given year, and that year's URCS is then applied two years later, *e.g.*, the 2013 URCS would be applied for the 2015 rates. AEPCO's approach adheres to this pattern.

The dynamic differs somewhat for the reparations period, *e.g.*, AEPCO's 2009 reparations were based on the 2009 URCS (unaffected by the PPA), and AEPCO's 2010 and 2011 reparations were based on the 2010 URCS (which also governed AEPCO's 2012 rates), as the 2011 URCS was not available at the time. Nonetheless, the fact that BNSF filed a PPA-tainted URCS for 2010-2012 provides no justification for substituting a later URCS that becomes available due to the time it took the Board to issue the *Declaratory Order*. In *OG&E*, the Board expressly "declined the parties' request to establish a 'true-up' process to account for the lag between the time when movements occur and when URCS costs for that specific time period become available." *OG&E* (STB served Oct. 26, 2009) at 2 (construing the July 24, 2009 *OG&E* decision).

The substitution of the corrected 2010-2011 URCS for the original URCS should apply to both the BNSF and the Western Regional URCS, which was used to calculate the costs for the SWRR segment.<sup>5</sup> Indeed, BNSF comprises half of the Western Regional URCS.<sup>6</sup> Failing to adjust the 2010-2011 Western Regional URCS for the improper PPA would provide the carriers with an unwarranted cost recovery.

AEPCO's approach is straightforward, easily implemented, achieves what would have been accomplished at the time if untainted data had been available, and conforms to the Board's *Declaratory Order* and *OG&E* procedures. It also allows BNSF

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<sup>5</sup> AEPCO's position is without prejudice to its pending appeal, where AEPCO contends that the SWRR segment should be treated as part of the BNSF segment.

<sup>6</sup> BNSF, with the PPA, accounts for 49.6% of the Western Region total costs and 50.1% of the Western Regional total variable costs for 2010 (URCS cells D8L613C1 and D8L614C1, respectively).



to receive the benefit of the PPA to the extent allowed under the *Declaratory Order* as the PPA is reported in BNSF's R-1 Reports and incorporated in the URCS formulas developed in accordance with the Board's established procedures.

#### **IV. BNSF'S POSITION**

In contrast, BNSF's position is complicated and consists largely of elements that have no support in, and are generally contrary to, the *Declaratory Order* and the *OG&E* procedures.

First, BNSF would substitute the corrected BNSF URCS from a later year for the original BNSF URCS for an earlier year; *e.g.*, the corrected 2011 BNSF URCS would replace the original 2010 BNSF URCS for 2011, and the corrected 2012 BNSF URCS would replace the original 2010 BNSF URCS for 2012 and 2013. However, nothing in the *Declaratory Order* supports or even contemplates this sort of displacement. While BNSF may believe that the more contemporaneous data should be used now that it is available, the Board rejected this sort of "true-up" approach in *OG&E*. The Board found that "[c]onvoluted interim rates and true-ups subject shippers to a great deal of risks and uncertainty as to the actual transportation rate that will ultimately be imposed on a given shipment" and "would force the shipper to ship under rates that would be always subject to later revision." *OG&E* (served July 24, 2009) at 10. The Board added that "indexing the best available URCS data [at the time] is a simple and unbiased approach," and explained that while "[t]he actual variable costs will inevitably be shown to be higher or lower ... there is no reason to conclude that the simple approach ... will systematically skew the variable cost estimate in favor of either the shipper or the

railroad.” *Id.*<sup>7</sup> Nothing in the *Declaratory Order* suggests any intent to displace the established *OG&E* procedures.

Second, BNSF would not extend any PPA correction to the Western Regional URCS for 2010-2011. However, since BNSF comprises roughly half of the Western Regional total and variable costs, the PPA should be removed from the Western Regional URCS as well as the BNSF URCS for that period. Otherwise, the cost treatment of the SWRR segment will reflect the PPA that the Board has excluded.

Third, BNSF contends that it is entitled to receive the benefit of the PPA in its rates starting in 2013. *See* Exhibit A (BNSF emails). However, the *Declaratory Order* states only that BNSF is to begin phasing in the PPA in its *R-1 Reports* starting 2013. *Id.* at 2, 29-31. The Board’s order gives no hint that the PPA is to be phased into BNSF’s *rates* starting in 2013. There is also no support for BNSF’s supposition that the Board intended any departure from the *OG&E* procedures in its *Declaratory Order*.

Fourth, because the *Declaratory Order* says nothing about how to effectuate a rate PPA phase-in starting 2013, BNSF is forced to concoct a mechanism for doing so, namely, deriving the average differential between the 2010/2011 URCS with and without the PPA, and then phasing in a portion of the differential beginning with the

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<sup>7</sup> The Board further explained that the *OG&E* mechanism “will provide certainty to the parties, avoid the expense of hiring consultants to perform an annual true-up, minimize ancillary disputes, and, in our judgment, strikes the proper balance between the desire for accuracy and the time, expense, and burden of waiting for more accurate costing data to become available.” *Id.* at 10-11. The Board was also concerned that “a decision to adopt any kind of true-up provision would apply to all our rail rate cases.” *Id.* at 10.

2013 rates.<sup>8</sup> Because the PPA is phased into the regular URCS costs starting in 2015 (which utilizes the 2013 URCS), BNSF devises a complicated reconciliation mechanism so that the “total” PPA phase-in amounts to 25% in 2013, 50% in 2014, 75% in 2015, and 100% in 2016-2018. *See* Exhibit A (letter from BNSF’s counsel dated Sept. 18, 2013).<sup>9</sup> However, the PPA differential, phase-in, and reconciliation find no support in the *Declaratory Order* and constitute the sort of “[c]onvolved ... true-up” that the Board rejected in *OG&E* (STB served July 24, 2009) at 10.

In short, there is no basis for adopting any element of BNSF’s position (except where it corresponds to that of AEPCO).

## **V. UP’S POSITION**

UP’s position addresses only 2010 and 2011 since there is no dispute as to 2009 (Berkshire acquired BNSF in 2010), and the carriers adopted proportional rates in 2012.<sup>10</sup> UP maintains that its 2011 URCS should be substituted for its 2010 URCS for

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<sup>8</sup> It is not immediately apparent whether the 2010/2011 differential should be based on a percentage or dollar variable cost or whether the differential calculated in 2010/2011 will be accurate several years later as some assets are retired, other assets are added, and such items as the cost of capital and productivity vary.

<sup>9</sup> For example, BNSF’s 100% phase-in for 2016 consists of 50% of the 2010/2011 differential and 50% of the PPA phase-in in the 2014 URCS that is applied during 2016. BNSF apparently recognizes that a 100% phase-in in 2016 occurring through the regular URCS would violate the *Declaratory Order*. However, in order to be able to submit a 2014 R-1 Report with a 50% phase-in, BNSF must have the data and know the adjustments that would be required to submit an R-1 Report with a full phase-in and with no phase-in. The 2010/2011 PPA differential is thus a device for avoiding the clear import of the *Declaratory Order*, and appears destined to be less accurate than recognizing the phase-in directly in the R-1 Reports and associated URCS.

<sup>10</sup> UP does not disclose what its position would be if the switch to proportional rates is overturned. AEPCO’s pending appeal also challenges the adoption of proportional rates.

use in 2011, and the same should occur for the Western Regional URCS (but without any correction for the PPA).

There is no support for UP's position. The BNSF PPA has nothing to do with UP. Nothing in the *Declaratory Order* gives any hint that the vintage of the UP URCS should be revised. Furthermore, the notion that the 2011 URCS should be used to determine the 2011 rates because the 2011 URCS is now available runs afoul of *OG&E*, as explained *supra*. BNSF's noncompliance with 49 U.S.C. § 11323 provides no justification for increasing UP's portion of the joint rates.

Perhaps even more perverse is UP's position that the original 2011 Western Regional URCS should replace the original 2010 Western Regional URCS for use in calculating the SWRR portion of the joint rates in 2011. The substitution of the later Western Regional URCS because it is now available violates *OG&E*. The larger problem, however, is that the original 2010 and 2011 Western Regional URCS are both tainted by the BNSF PPA. Indeed, BNSF, with the PPA, accounts for about half of the 2010 URCS. The appropriate change is to replace the original 2010 Western Regional URCS with the corrected 2010 Western Regional URCS for use in both 2010 and 2011 (as the 2010 URCS was originally utilized to calculate AEPCO's 2010 and 2011 reparations), so as to remove the impact of the BNSF PPA that the Board rejected in the *Declaratory Order*.

## **VI. CONCLUSION**

The Board should reinstate the rate prescription and adopt AEPCO's approach for implementing the prescription as AEPCO's approach conforms to the

Board's *Declaratory Order* and *OG&E* procedures, is simple and straightforward (especially in contrast to the BNSF and UP proposals), and is easily implemented. The Board should reject BNSF's and UP's approaches as they have no support in the *Declaratory Order*, run afoul of the *OG&E* procedures, are complicated and convoluted, and yield perverse results.

Respectfully submitted,

ARIZONA ELECTRIC POWER  
COOPERATIVE, INC.

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Dated: September 23, 2013

Attorneys & Practitioners

CERTIFICATE OF SERVICE

I hereby certify that on this 23rd day of September, 2013, I caused copies of the foregoing filing to be served on counsel for Defendants Union Pacific Railroad Company and BNSF Railway Company by email and hand as follows:

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and by email and overnight courier to:

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/s/ Robert D. Rosenberg

## EXHIBIT A

Email Exchanges Among Counsel for AEPCO, BNSF, and UP  
Regarding Implementation of the Board's *Declaratory Order*

## Robert Rosenberg

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**From:** Rosenthal, Michael <mrosenthal@cov.com>  
**Sent:** Monday, September 16, 2013 10:33 AM  
**To:** LaRocca, Anthony; Robert Rosenberg; Louise A. Rinn [LARINN@up.com] (LARINN@up.com)  
**Cc:** Sipe, Samuel; Rosenthal, Michael  
**Subject:** RE: AEPCO prescription/rates and BNSF acquisition markup

Robert and Tony:

UP's view is that, if the Board is going to revisit the reparations due to AEPCO for the period in which there was a joint rate, it should not only use the revised 2010 and 2011 BNSF URCS, but it should also use the most accurate cost information available for UP and SWRR. This means: (1) for 2010, revised 2010 BNSF URCS and existing 2010 UP and Western Region URCS; (2) for 2011, revised 2011 BNSF URCS and existing 2011 UP and Western Region URCS. Unless the DC Circuit reverses the Board's decision allowing UP to establish proportional rates in 2012 and beyond, the years after 2011 are not of concern to UP. (And, even if the DC Circuit were to reverse the decision, UP still might not have any concern, depending on what the court says and what the Board does.)

Regards,

Mike

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**From:** LaRocca, Anthony [mailto:ALaRocca@steptoe.com]  
**Sent:** Friday, September 13, 2013 3:27 PM  
**To:** Robert Rosenberg; Rosenthal, Michael; Louise A. Rinn [LARINN@up.com] (LARINN@up.com)  
**Cc:** Sipe, Samuel  
**Subject:** RE: AEPCO prescription/rates and BNSF acquisition markup

Robert: I am responding to your September 11, 2013 e-mail initiating discussions on approaches for reinstituting the rate prescription in Docket No. NOR 42113 pursuant to the Board's July 25, 2013 decisions in Docket No. NOR 42113. We have several concerns with your proposed approach.

First, to determine the appropriate amount of reparations due to AEPCO for the period 2010/2011, the jurisdictional threshold for those two years needs to be recalculated. As you note in your e-mail, the Board will be issuing revised 2010 and 2011 BNSF URCS after receiving revised R-1 reports from BNSF that exclude the asset markup resulting from the Berkshire Hathaway acquisition of BNSF. Thus, the 2010 URCS will be available to recalculate the jurisdictional threshold for 2010 and the 2011 URCS will be available to recalculate the jurisdictional threshold for 2011. There is no reason to continue using an outdated 2010 URCS to recalculate the jurisdictional threshold for 2011, as you propose, when a 2011 URCS will be available.

Second, you propose to continue using an outdated 2010 URCS indexed to 2012 to recalculate the jurisdictional threshold for 2012. However, as you acknowledge in your e-mail, the Board has instructed BNSF to submit a new R-1 report for 2012 that excludes the asset markup resulting from the Berkshire Hathaway acquisition of BNSF. The Board will issue a new 2012 BNSF URCS that excludes



the markup, probably around the same time that it will issue revised 2010 and 2011 BNSF URCS. Since a valid 2012 URCS will be available to determine the jurisdictional threshold, there is no reason to continue using the 2010 URCS.

Third, you suggest that the Board intends to reissue the Western Region URCS along with revised BNSF URCS for 2010 and 2011. The Western Region URCS is used to determine the Southwest Railroad (SWRR) variable costs. We have no reason to believe that the Board intends to issue a revised Western Region URCS for 2010 and 2011, nor do we read the Board's July 25, 2013 decision in FD 35506 or in NOR 42113 as requiring any adjustment to the Western Region URCS for the historical time period. We believe the recalculation of variable costs should be limited to BNSF's portion of the movement. Indeed, if we were to modify the costs calculated for the SWRR, it would also be necessary to modify the 2011 costs for the UP since we now have a 2011 UP URCS.

Fourth, the Board has allowed BNSF to capture 25% of the asset markup resulting from Berkshire Hathaway's acquisition in BNSF's variable costs starting in 2013 as part of a four-year transition to full recognition of the markup. In contrast, you propose that no portion of the asset markup will be reflected in BNSF's rates until 2015. To reflect 25% of the asset markup in the rates for 2013, we propose the following approach: (1) BNSF's variable costs for the AEPCO movement would first be calculated using BNSF's 2012 URCS which excludes the effect of the asset markup; (2) the incremental variable costs of the AEPCO movement associated with the asset markup would be calculated by comparing the variable costs for the AEPCO movement in 2010 and 2011 using the 2010 and 2011 URCS that include the asset markup and the revised 2010 and 2011 URCS that exclude the asset markup; (3) one quarter of the incremental cost determined in Step 2 above would be added to the variable costs calculated in Step 1 above to determine the jurisdictional threshold rate. For future years, this methodology could be used to ensure that an increasing amount of the asset markup is reflected in BNSF's variable costs over the transition period.

We expect that it will be necessary to discuss these issues in person. Please advise when you are available to discuss. Tony

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**From:** Robert Rosenberg [<mailto:rdr@sloverandloftus.com>]

**Sent:** Wednesday, September 11, 2013 1:14 PM

**To:** LaRocca, Anthony; Mike Rosenthal ([mrosenthal@cov.com](mailto:mrosenthal@cov.com)); Louise A. Rinn [[LARINN@up.com](mailto:LARINN@up.com)]

**Subject:** AEPCO prescription/rates and BNSF acquisition markup

Tony, Mike, and Lou Anne:

The STB's July 24, 2013 decision directs AEPCO and Defendants BNSF and UP to confer on approaches to reinstituting the rate prescription and to advise the STB by September 23, 2013. Please consider this note as initiating the discussion. We would be pleased to confer by telephone, but this matter has enough parts that we thought an email would be the better way to tee things up.

The STB has directed BNSF to file corrected R-1 reports for 2010-2012 by September 23, 2013. We expect that the STB will then prepare the corrected URCS formulas for both BNSF and the Western Region (SWRR) for 2010-2011 and the URCS formulas for 2012. Since the 2010 URCS formulas were used to calculate AEPCO's reparations for 2010-2011, we expect that the corrected 2010 URCS formulas will be used to calculate additional reparations due AEPCO for 2010 and 2011. Since the 2010 URCS formulas were also used to calculate

AEPCO's rates for 2012 and the first weeks of 2013, the corrected 2010 URCS formulas will also be used to calculate additional reparations due AEPCO for 2012 and the first weeks of 2013. Since the 2011 URCS formulas were used to calculate AEPCO's rates for the remainder of 2013, the corrected 2011 URCS formulas will be used to calculate additional reparations due AEPCO for the remainder of 2013 and the first weeks of 2014. The reparations for 2011-2014 will include interest. Assuming the 2012 URCS formulas are available on a timely basis, they will be used to calculate AEPCO's rates for the remainder of 2014 and the first weeks of 2015. If they are not available on a timely basis, it may be necessary to continue to utilize the 2011 URCS formulas, subject to additional reparations when the correct URCS formulas become available.

We understand that BNSF will begin phasing-in the acquisition write-up with the 2013 R-1. If so, we would expect one-quarter of the write-up to be reflected in the 2013 URCS formulas, which would be expected to be reflected in AEPCO's rates after the first few weeks of 2015. The 2014-2016 URCS formulas will follow in turn for use during 2016-2018.

We do not view any of the above as altering the prescription, which is, and remains, at the jurisdictional threshold of 180% of variable costs. Instead, we view the corrected R-1 reports as resulting in corrected variable costs. Also, we recognize that BNSF and UP implemented proportional rates starting January 1, 2012. Accordingly, the corrected URCS formulas will apply only to the BNSF rates starting that date, contingent upon the outcome of AEPCO's appeal. (We note that AEPCO's appeal could also result in the non-use of the Western Region URCS formula for the SWRR segment.) We believe the report to be filed with the STB should be from AEPCO and both defendants.

If the carriers believe that "refunds" is a more appropriate term than "reparations," please let us know. In addition, please let us know if the carriers believe it necessary to obtain a formal STB order directing the payment of the additional reparations/refunds. Regardless, an order reinstating the prescription that was temporarily lifted by the January 20, 2012 decision also appears to be necessary.

We look forward to hearing from you.

Robert

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## Robert Rosenberg

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**From:** LaRocca, Anthony <ALaRocca@steptoe.com>  
**Sent:** Wednesday, September 18, 2013 12:08 PM  
**To:** Robert Rosenberg  
**Cc:** Mike Rosenthal (mrosenthal@cov.com); Sipe, Samuel  
**Subject:** AEPCO

Robert: You asked me to clarify the approach that BNSF is proposing for adjusting BNSF's prescribed rates in 2014-2018 to account for the increasing amount of the asset markup that BNSF is entitled to reflect in its variable costs. My September 13 e-mail to you described the approach that we propose for 2013, when BNSF is entitled to account for 25% of the asset markup. In 2014, BNSF is entitled to account for 50% of the asset markup as part of the four-year transition to a full recognition of the asset markup. The variable cost calculations for 2014 will be based on the 2012 URCS, which will be the most current available URCS. However, the 2012 URCS will not include any effect of the markup. My September 13 e-mail described the methodology for determining the variable cost associated with the asset markup (using the 2010/2011 URCS with and without the asset markup). For 2014, one-half of that markup-related variable cost would be added to the BNSF variable costs determined using the 2012 URCS to ensure that one-half of the asset markup is accounted for in 2014. For 2015, the BNSF variable cost calculations will be based on the BNSF 2013 URCS, which will include 25% of the asset markup. However, in 2015, BNSF is entitled to account for 75% of the asset markup as part of the transition to full recognition of the asset markup. Therefore one-half of the markup-related variable cost (determined as described in my September 13 e-mail) would be added to the 2015 BNSF variable costs determined using the 2013 URCS to ensure that 75% of the asset markup is reflected in the jurisdictional threshold rates (25% plus 50%). For 2016, the BNSF variable cost calculations will be based on BNSF's 2014 URCS, which will include 50% of the asset markup. However, in 2016, BNSF is entitled to account for 100% of the asset markup. Therefore one-half of the markup-related variable cost would be added to the 2016 BNSF variable costs determined using the 2014 URCS to ensure that 100% of the asset markup is reflected in the jurisdictional threshold rates (50% plus 50%). For 2017, the BNSF variable cost calculations will be based on BNSF's 2015 URCS, which will include 75% of the asset markup. However, in 2017, like 2016, BNSF is entitled to a full recognition of the asset markup. Therefore one-quarter of the markup-related variable cost would be added to the 2017 BNSF variable costs determined using the 2015 URCS to ensure that 100% of the asset markup is reflected in the jurisdictional threshold rates (25% plus 75%). Finally, BNSF's variable costs for 2018, the last year of the rate prescription, will be based on 2016 URCS, which will fully reflect the asset markup, and no adjustment is required. Please advise if you need further clarification of the proposed methodology. Tony

## EXHIBIT B

Table Comparing Original Treatment and  
AEPCO, BNSF, and UP Positions on Purchased Price Adjustment (“PPA”)

# EXHIBIT B

Comparison of Original Treatment and AEPCO and BNSF and UP Positions on Purchased Price Adjustment ("PPA")				
Year	Original	AEPCO Position	BNSF Position	UP Position
2009	Orig. 2009 BNSF URCS Orig. 2009 Western URCS (SWRR) Orig. 2009 UP URCS	Unaffected	Unaffected	Unaffected
2010	Orig. 2010 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2010 BNSF URCS Corrected 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2010 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2010 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS
2011	Orig. 2010 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2010 BNSF URCS Corrected 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2011 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2011 BNSF URCS Orig. 2011 Western URCS (SWRR) Orig. 2011 UP URCS
2012	Orig. 2010 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2010 BNSF URCS Corrected 2010 Western URCS (SWRR) Orig. 2010 UP URCS	Corrected 2012 BNSF URCS Orig. 2010 Western URCS (SWRR) Orig. 2010 UP URCS	No position (contingent on D.C. Circuit)
2013	Orig. 2011 BNSF URCS Orig. 2011 Western URCS (SWRR) Orig. 2011 UP URCS	Corrected 2011 BNSF URCS Corrected 2011 Western URCS (SWRR) Orig. 2011 UP URCS	Corrected 2012 BNSF URCS (plus 1/4 2010/2011 PPA differential*) Orig. 2011 Western URCS (SWRR) Orig. 2011 UP URCS	No position (contingent on D.C. Circuit)
2014	Orig. 2012 BNSF URCS Orig. 2012 Western URCS (SWRR) Orig. 2012 UP URCS	Corrected 2012 BNSF URCS Corrected 2012 Western URCS (SWRR) Orig. 2012 UP URCS	Corrected 2012 BNSF URCS (plus 1/2 2010-2011 PPA differential *) Orig. 2012 Western URCS (SWRR) Orig. 2012 UP URCS	No position (contingent on D.C. Circuit)
2015	Orig. 2013 BNSF URCS Orig. 2013 Western URCS (SWRR) Orig. 2013 UP URCS	Orig. 2013 BNSF URCS Orig. 2013 Western URCS (SWRR) Orig. 2013 UP URCS	Orig. 2013 BNSF URCS (plus 1/2 2010/2011 PPA differential*) Orig. 2013 Western URCS (SWRR) (includes 1/4 BNSF PPA*) Orig. 2013 UP URCS	No position (contingent on D.C. Circuit)
2016	Orig. 2014 BNSF URCS Orig. 2014 Western URCS (SWRR) Orig. 2014 UP URCS	Orig. 2014 BNSF URCS Orig. 2014 Western URCS (SWRR) Orig. 2014 UP URCS	Orig. 2014 BNSF URCS (plus 1/2 2010/2011 PPA differential*) Orig. 2014 Western URCS (SWRR) (includes 1/2 BNSF PPA*) Orig. 2014 UP URCS	No position (contingent on D.C. Circuit)
2017	Orig. 2015 BNSF URCS Orig. 2015 Western URCS (SWRR) Orig. 2015 UP URCS	Orig. 2015 BNSF URCS Orig. 2015 Western URCS (SWRR) Orig. 2015 UP URCS	Orig. 2015 BNSF URCS (plus 1/4 2010-2011 PPA differential*) Orig. 2015 Western URCS (SWRR) Orig. 2015 UP URCS	No position (contingent on D.C. Circuit)
2018	Orig. 2016 BNSF URCS Orig. 2016 Western URCS (SWRR) Orig. 2016 UP URCS	Orig. 2016 BNSF URCS Orig. 2016 Western URCS (SWRR) Orig. 2016 UP URCS	Orig. 2016 BNSF URCS Orig. 2016 Western URCS (SWRR) Orig. 2016 UP URCS	No position (contingent on D.C. Circuit)
<p>Notes:</p> <p>2009-2011 constitutes original Reparations Period. BNSF and UP adopted proportional rates effective January 1, 2012. The Board has not yet issued an URCS for 2012. Original 2012 BNSF and Western Regional URCS refer to the URCS which would have reflected the original 2012 BNSF R-1, and Corrected 2012 BNSF and Western Regional URCS refer to the URCS that reflects the corrected BNSF R-1 for 2012.</p> <p>* BNSF determines a 2010/2011 PPA differential based on comparison of 2010 and 2011 variable costs with and without PPA and applies 25% of the PPA differential in 2013 and 2017 and 50% in 2014, 2015, 2016. In addition, the PPA is phased in under the Original URCS for 2013-2016 at 25% per year (25% in 2013, 50% in 2014, 75% in 2016, and 100% in 2017).</p>				